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Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554

FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

In the matter of

Amendment of the Commission's Rules to Utilize  
Competitive Bidding for Licenses, pursuant to the  
Omnibus Budget Reconciliation Act of 1993

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Gen. Docket 93-\_\_\_\_  
RM-\_\_\_\_

PETITION FOR RULEMAKING

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September 14, 1993

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## EXECUTIVE SUMMARY

In Title VI of the Omnibus Budget Reconciliation Act of 1993, Congress authorized the Commission to begin using competitive bidding for licensing commercial radio services. In this petition, BellSouth sets forth its proposals for auctioning licenses in new services such as PCS.

BellSouth urges the Commission to use an established auction house and to use an open auction, rather than a sealed-bid process. Open auctions are the simplest form of auction to implement. They will also recover more of the value of the spectrum than sealed bids and will reward the highest-valued use of the spectrum. An open auction is particularly appropriate when, as in PCS, (a) the interested bidders differ significantly in their willingness to risk not winning the auction, (b) the bidders are all seeking to determine the objective commercial value of the license, and (c) there are several different sets of bidders with differing probable valuation ranges for the license. Open bidding would also further the Congressional objective of encouraging competition and opening services such as PCS up to a wide variety of businesses, including minority- and female-owned businesses and rural telephone companies. An open auction provides a flow of information to bidders that would be particularly beneficial to new entrants attempting to put a value on a license. The Commission could also enhance the opportunities for a wide variety of businesses to bid on PCS licenses by widely publicizing the PCS auction process. To ensure that only *bona fide* bidders participate, the Commission should require bidders to post a reasonable deposit, scaled to the size of the population in a service area.

Licenses should be auctioned separately, in decreasing population order. Auctioning the licenses that will serve the largest populations first would be responsive to the expected high level of demand for service in these markets. BellSouth suggests that the licenses for serving a given area should be equivalent in geographic scope and amount of spectrum, in order to maximize opportunities for new entry and competition and to avoid consigning many bidders, such as small and minority-owned businesses, to the least valuable licenses.

The winning bidder should, in all cases, be given the option of paying the bid amount in a lump sum or in installments. The Commission should adopt rules specifying the terms of permitted installment plans. Payments should extend over no more than five years, to ensure that revenues are recovered during Fiscal Years 1994-98. The Commission should not impose significant restrictions on assignments of licenses and transfers of control. Holding periods and similar "antitrafficking" restrictions would interfere with economically efficient spectrum usage. Assignment and transfer applications should be reviewed, however, to prevent unjust enrichment or other auction abuses. The Commission should make clear that licensees who do not meet any reasonable construction and coverage requirements established for PCS will forfeit their licenses, unless there is good cause for their failure. Moreover, forfeiture of a license should not relieve a licensee from responsibility for completing payment of the bid amount, if it has taken advantage of an installment payment plan.

Finally, to carry out the Congressional objective of minimizing administrative and judicial delay, BellSouth recommends that the Commission reinvent the licensing process for PCS, eliminating all unnecessary sources of delay.

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**PETITION FOR RULEMAKING**

BellSouth Corporation, BellSouth Telecommunications, Inc., and BellSouth Enterprises, Inc. (collectively, "BellSouth"), by their attorneys, hereby petition the Commission to issue a notice of proposed rulemaking to establish rules and regulations for conducting competitive bidding for licenses, pursuant to Title VI of the Omnibus Budget Reconciliation Act of 1993 ("OBRA"), Pub. L. No. 103-66, 107 Stat. \_\_\_\_ (Aug. 10, 1993).<sup>1</sup> As shown below, open bidding is the proper auction mechanism to employ for the efficient assignment of PCS licenses

**INTRODUCTION**

In the PCS docket, BellSouth advocated the use of auctions for licensing new personal communications services and proposed both legislation and rules to facilitate competitive bidding.<sup>2</sup> BellSouth now encourages the Commission to adopt rules for open bidding on PCS licenses.

Congress has now enacted legislation authorizing the use of the competitive bidding process for a variety of services.<sup>3</sup> Under Title VI of OBRA, the Commission is required to conclude a

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<sup>1</sup> See also H.R. Rep. 103-213, 103d Cong. 1st Sess., 103 Cong. Rec. H5792 (Aug. 4, 1993) ("Conference Report").

<sup>2</sup> PCS Comments of BellSouth at 55-62, filed November 9, 1992, in response to the Commission's *Notice of Proposed Rulemaking and Tentative Decision* in Gen. Docket 90-314, *New Personal Communications Services*, 7 FCC Rcd. 5676 (1992) ("PCS Comments").

<sup>3</sup> OBRA § 6003(a) amends Section 309 of the Communications Act, 47 U.S.C. § 309, by adding new § 309(j), "Use of Competitive Bidding."

general rulemaking to implement this legislation no later than March 8, 1994.<sup>4</sup> The statute also requires the Commission to begin issuing PCS licenses before May 7, 1994.<sup>5</sup> BellSouth is filing this petition for rulemaking to assist the Commission in meeting these requirements.

In this petition, BellSouth proposes the adoption of rules and policies to govern competitive bidding for licenses in PCS and similar new services. PCS meets the criteria Congress established for services to subject to competitive bidding.<sup>6</sup> As BellSouth explains herein, the Commission should use open bidding for PCS licenses.

### **THE PROPOSED RULEMAKING**

BellSouth proposes that the Commission use open bidding as its standard auction technique for new services, including PCS. The bidding process should be conducted by an organization experienced in auctioning a wide variety of valuable properties. This means of competitive bidding would be simple, fair, and efficient. It would also satisfy all of the objectives set by Congress for design of competitive bidding systems.

The Commission should also make the determination, pursuant to Section 309(j)(2), that PCS constitutes a use of spectrum for which auctions are appropriate. Specifically, BellSouth proposes the following auction system for licenses in new services subject to competitive bidding, and in particular for PCS:

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<sup>4</sup> OBRA § 6003(d)(1) provides that the FCC "shall prescribe regulations to implement section 309(j) of the Communications Act of 1934 (as added by this section) within 210 days after the date of enactment of this Act."

<sup>5</sup> OBRA § 6003(d)(2)(B) provides that "the Commission shall -- . . . within 270 days after such date of enactment, commence issuing licenses and permits in the personal communications service."

<sup>6</sup> Before the Commission may use competitive bidding for a particular "class of licenses," it must make a determination that certain criteria are met. Specifically, the Commission must determine for each class of licenses, that (1) the principal use of the spectrum involved is likely to involve the licensee being paid by subscribers for being able to receive or transmit information on the licensee's frequencies, and (2) the use of competitive bidding will promote the statutory objectives set forth in § 309(j)(3). See 47 U.S.C. § 309(j)(2)(A)-(B).

- Use open bidding at auctions conducted by an experienced auctioneer under contract.
- Hold auctions sequentially, auctioning the licenses for the most populous areas first.
- Provide opportunities to a variety of businesses through an open, well-publicized process, reasonable application criteria, and availability of an installment payment plan, instead of bidding preferences or other special preferential procedures.
- Require bidders to file an abbreviated initial application shortly before a scheduled auction.
- Review applications for acceptability promptly and issue a public notice listing those who are eligible to bid.
- Require bidders to post a reasonable deposit.
- Issue a public notice immediately after the auction announcing the winning bidder and the price bid.
- Require the winning bidder to submit an amended application containing more detailed information within 15 days after the public notice, with petitions to deny due 30 days after the amendment deadline.
- Require the winning bidder to pay the bid amount within seven days of being found qualified, either in a lump sum or by signing a note for installment payments (if installment payments are selected, any license issued should be conditioned on satisfaction of the payment obligation).
- Require licensees to comply with reasonable minimum build-out requirements, with forfeiture of license upon failure to meet these requirements, absent good cause.
- Permit transfers of control and assignments of licenses, subject to approval under Section 310(d), without any "holding period," construction requirement, or other restraints on alienation. Any assignment of license should be conditioned on prior satisfaction of any remaining installment payments; in the alternative, both assignor and assignee should be liable for any remaining installment obligations.

## DISCUSSION

### I. OPEN BIDDING IS MOST APPROPRIATE FOR NEW SERVICES SUCH AS PCS

The first issue the Commission must decide is what kind of auction process to use. There are two principal types of auctions that may be appropriate: the open auction and the sealed-bid auction.<sup>7</sup> There are many variants on these basic types of auctions, as well as techniques that may be used in conjunction with them, such as setting reserve prices.

Congress did not select any single auction type in granting the Commission auctioning authority. Indeed, it encouraged the Commission to test different techniques "in appropriate circumstances."<sup>8</sup> However, Congress did require the Commission to establish a particular auction process by rule for each "class of licenses" subject to auctions.<sup>9</sup>

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<sup>7</sup> In an open, or "English," auction, bidders raise the bid price until only one bidder remains; the last bidder pays the price it bid. In a first-price sealed bid auction (referred to herein as a "sealed bid" auction), sealed bids are submitted; the highest bidder wins and pays the price it bid. See generally R.P. McAfee and J. McMillan, *Auctions and Bidding*, 25 J. Econ. Lit. 699, 702 (June 1987).

There are two other basic types of auction: the second-price sealed bid ("Vickrey") auction, in which sealed bids are submitted and the highest bidder wins, paying the price bid by the second-highest bidder; and the descending-price ("Dutch") auction, in which the auctioneer descends from a high price until the first bidder accepts the bid. *Id.* On average, open auctions and second-price sealed-bid auctions will yield the same price; similarly, the descending-price auction and the first-price sealed-bid auction will generally result in the same price. See J.G. Riley & W.F. Samuelson, *Optimal Auctions*, 71 Amer. Econ. R. 381, 382 & n.4 (June 1981). Accordingly, there does not appear to be any significant reason for the Commission to consider these additional types of auctions.

The theoretical equivalence of sets of auction techniques on average does not mean that in every instance the two equivalent techniques will yield identical results. In particular, a small number of bidders can cause anomalous results. For example, in New Zealand a second-price sealed-bid auction was used to award a UHF television license without any reserve price. Only two bids were submitted. The winning bidder bid NZ\$100,004 but only had to pay the amount of the second bid, NZ\$6. See Congressional Budget Office, *Auctioning Radio Spectrum Licenses* 46 (March 1992). The final bid in an open auction would clearly have been higher than NZ\$6.

<sup>8</sup> 47 U.S.C. § 309(j)(3).

<sup>9</sup> *Id.*

In identifying the classes of licenses and determining the type of auction to use for a particular class of licenses, Congress required the Commission to promote several objectives. These can be summarized as follows: (A) avoidance of delay in making new technologies, products and services available; (B) making licenses for using new and innovative technologies available to a wide variety of applicants in order to promote economic opportunity and competition and avoid excess concentration; (C) recovery of revenues for spectrum resources used commercially and avoidance of unjust enrichment; and (D) encouragement of spectral efficiency.<sup>10</sup>

Consistent with these objectives, the Commission should adopt auction rules for the following class of licenses:

Licenses in new radio services or new spectrum allocations that permit the licensee to utilize advanced technology to provide varied voice, data, or video services to a large number of subscribers.

The broad definition of this class of licenses is appropriate because all such licenses share the same characteristics from the viewpoint of the statutory objectives.<sup>11</sup>

**A. An Open Bidding Process Has Distinct Advantages for Licensing New Services Such as PCS**

Open auctions have distinct advantages for awarding licenses in new, broadly defined radio services where the licensee has the discretion to select an appropriate technology and to determine

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<sup>10</sup> 47 U.S.C. § 309(j)(3)(A)-(D).

<sup>11</sup> Objective (C) is particularly well-served by using a single auction technique for this broadly defined class of licenses. These licenses are similar with respect to the economic assumptions that must be made in designing an auction technique, as discussed in the following section. Objective (D) of the statute will also be served by defining the class as proposed. An auction technique that rewards the winning bidder for being able to use spectrum efficiently and intensively will be effective in nearly all new services.

Objective (A) is also served by this class definition: All of these licenses enable the development and deployment of new technologies, products and services. An auctioning method that avoids delays in licensing will be equally effective in allowing all such licensees to get on with the business of providing their services.

Finally, adopting the proposed broadly defined class of licenses will serve objective (B). All of the licenses in this proposed class will provide similar opportunities for participation by a wide variety of entrants and make new technologies readily accessible to the public.



the products and services it offers to the public.<sup>12</sup> For this class of licenses, and for PCS in particular, BellSouth urges the Commission to conduct open auctions.

**1. Open Bidding Will Recover the Value of Spectrum, Prevent Unjust Enrichment, and Encourage Efficient Spectrum Use**

Open bidding is preferable to sealed bids because it is likely to serve the statutory objective of recovering for the public the value of the spectrum and preventing unjust enrichment. Moreover, it will reward the bidder who most highly values the spectrum, which will result in incentives to utilize spectrum most efficiently and intensively.

Different types of auctions may be more or less efficient in reaching a sale price reflecting the value of the spectrum, depending on the characteristics of the buyers and how they value the good to be sold. There are three key characteristics of bidders that will affect the choice of an auction technique: (1) the bidders' attitude toward the risk of failing to win an auction; (2) whether the bidders value the license based on its unique private value to them individually, or instead based on their perceptions of a value it has to all bidders in common; and (3) whether the bidders can be categorized as a single class or several classes for purposes of the range of values that they might assign to the license.<sup>13</sup> Thus, to make an informed choice of an auction mechanism for new radio services such as PCS, the Commission must determine what assumptions to make regarding the bidders. In fact, the very nature of these new radio services makes it relatively easy to make these determinations.

First, the bidders will vary in terms of their adversity to the risk of failing to win an auction. Bidders that have already committed a substantial investment to entering the service in a particular

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<sup>12</sup> Any grant of discretion to licensees must be consistent with the requirements of Sections 301, 303, and 307 of the Act, which require the Commission to exercise control over the use of spectrum and establish basic parameters for spectrum use consistent with the public interest. Section 309(j)(6), added by OBRA, makes clear that the Commission's auction authority does not change these requirements.

<sup>13</sup> *Auctions and Bidding* at 704-06.

market will be risk-averse, as will those who conclude that their entry into the new service in a particular market is essential to their business goals because of related endeavors. Other bidders, however, will be risk-neutral with regard to winning a particular license.

If all bidders, or at least all of the high bidders, are risk-averse, a sealed-bid auction would be likely to yield a higher sale price. If all bidders were risk-neutral, the two methods would be essentially equivalent. However, an open auction would appear more likely to yield the highest price if risk-averse bidders face risk-neutral bidders who value the license higher going into the auction. In an open auction, when a "wild card" bidder unexpectedly raises the bid of the risk-averse bidder, the risk-averse bidder would have an incentive to reassess its own valuation and continue bidding higher, to increase the likelihood of winning the auction. This would not occur in a sealed-bid auction, however. Thus, the mixture of risk-averse and risk-neutral bidders appears to favor an open auction.

Second, a license for commercial use of radio spectrum has an objective commercial value that is ultimately based on its income-producing potential. That value cannot be known with any precision, when the license is for a new service with broad parameters. This is because there are few meaningful benchmarks for determining the value of a license whose ultimate utility is yet to be discovered. The bidders may therefore diverge considerably in their estimation of the license value, at least at the outset. These differing valuations do not represent private, independent values of the license unique to each bidder, however. The license will have an objective resale value that is dependent on the valuation of other potential licensees and is therefore common to all bidders.

Because each bidder estimates that objective common value from a different viewpoint, the bidders' initial valuations may be divergent. Under these circumstances, an open auction will generally yield a higher price than a sealed-bid auction. In a sealed-bid auction, the bidders do not have access to information about other bidders' estimates of the license's value. In an open auction, however, the bidders are constantly able to reassess their valuation based on the information gleaned

from others' bids. The open bidding process thus provides an information flow that permits low bidders to revise their valuations upward when they find that other bidders have estimated the license to have a higher value.<sup>14</sup> Accordingly, the open auction will tend to recover more of the value of the license for the public and avoid unjustly enriching the high bidder.

Third, the bidders are likely to fall into two or more classes with respect to their probable range of valuations. This factor favors open auctions over sealed-bid auctions. Certain bidders will have a higher probable valuation range than others because they possess, or believe they possess, cost advantages over the other bidders.<sup>15</sup> Sealed-bid auctions are inefficient under these circumstances. The bidder with the highest valuation will not necessarily prevail over the bidder with the next-highest valuation, if they fall in different classes, because their bids will not relate to their valuations in the same way. In an open auction, this will not prevent the price from ascending to the second-highest valuation, because the bidder with the highest value will continue bidding at least until that point. In a sealed-bid auction, however, there is an increased likelihood that the auction will result in a sale at a price lower than the second-highest valuation.

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<sup>14</sup> The information flow in an open auction also mitigates the "winner's curse" phenomenon that can occur in a sealed-bid auction for goods of uncertain common value. The high bidder, in the absence of information about others' valuations, will have estimated the value higher than all others, and thus may be unrealistically high. Bidders try to avoid this by adjusting their bids downward, but where there is considerable uncertainty as to the value, there may be a substantial difference between the highest and second-highest bids. In an open auction, the bidder with the highest valuation pays no more than the second-highest valuation, eliminating this difference. Thus, the value of the license is determined with greater certainty in an open auction. *See Auctioning Radio Spectrum Licenses* at 45. Moreover, this does not necessarily result in a lower price. The interdependence of the bidders' valuations means that the bids in an open auction "have the effect of making public each bidders' private information about the item's true value, thus lessening the effect of the winner's curse. As a result: *When bidders' valuations are affiliated, the English [open] auction yields a higher expected revenue than the first-price sealed-bid auction . . .*" *Auctions and Bidding* at 722 (emphasis in original).

<sup>15</sup> A company may, for example, believe that it has a cost advantage over other bidders because of its background in other businesses, its research and development efforts, or its particular technological approach, service philosophy, marketing technique, or other distinguishing characteristic.

Thus, the characteristics of the bidders for licenses in these new services suggest that an open auction would yield a higher price than a sealed-bid auction.<sup>16</sup> This advantage to the open auction would be diminished, however, if there were collusion among bidders. It has been suggested that open auctions are more conducive to such collusion.<sup>17</sup> For that reason, some have suggested that licenses should be auctioned by sealed bids.<sup>18</sup>

There are substantial reasons for not using the possibility of collusion as the basis for selecting one form of auction over another, however. First, bid-rigging and other forms of collusive bidding constitute *per se* violations of the Sherman Act, 15 U.S.C. § 1.<sup>19</sup> The Commission cannot reasonably base its decision on the presumption that if open bidding is selected, the many substantial companies interested in participating in PCS would be likely to engage in criminal collusion. Second, the companies who have already demonstrated an interest in PCS -- including telephone companies, cable television operators, cellular carriers, SMRs, and independent entrepreneurs -- are approaching PCS from so many different backgrounds, with different corporate cultures and different potential uses, that collusion is very unlikely.

An open eligibility policy such as BellSouth has urged would tend to preserve this diversity and minimize the opportunities for collusion. Moreover, if the Commission encourages all businesses to participate (consistent with the objectives set by Congress), collusion becomes even less likely. Under these circumstances, the interests of bidders will be highly divergent.

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<sup>16</sup> Appendix A contains a more detailed discussion of the rationale for using open auctions to maximize recovery of value in issuing licenses.

<sup>17</sup> *Auctions and Bidding* at 724; *Auctioning Radio Spectrum Licenses* at 45.

<sup>18</sup> *Auctioning Radio Spectrum Licenses* at 44-45, 46; see also E. Kwerel & A.D. Felker, *Using Auctions to Select FCC Licensees*, OPP Working Paper 16 at 22 (May 1985).

<sup>19</sup> *United States v. Flom*, 558 F.2d 1179, 1183 (5th Cir. 1977); see *United States v. Finis P. Ernest, Inc.*, 509 F.2d 1256 (7th Cir.), cert. denied, 423 U.S. 874, 893 (1975); *United States v. Bensinger Co.*, 430 F.2d 584 (8th Cir. 1970); *United States v. Pennsylvania Refuse Removal association*, 357 F.2d 806 (3rd Cir.), cert. denied, 384 U.S. 961 (1966); see also *Addyston Pipe and Steel Co. v. United States*, 175 U.S. 211 (1899).

A cartel must be able to coordinate its activities and punish violations,<sup>20</sup> which would not be possible under these circumstances. Thus, there is little likelihood that a bidding cartel would be able to operate.<sup>21</sup> Accordingly, the possibility of collusion should not be a basis for choosing one form of auction over another. Finally, under OBRA, collusion does not take on the same importance as it would under other auction regimes.<sup>22</sup>

Accordingly, the use of open auctions appears to be most beneficial with respect to the objective of recovering for the public the value of spectrum conferred by a license and thereby preventing unjust enrichment.

## **2. Open Auctions Will Best Serve the Statutory Objective of Providing Opportunities for Participation by a Wide Variety of Businesses**

Open auctions are also preferable to sealed-bid auctions in furthering the objective of facilitating participation by a wide variety of businesses, such as small businesses, minority- and female-owned businesses, and rural telephone companies.<sup>23</sup>

The open auction reveals information about the bidders and their evaluations that would be of great importance to companies new to a field. This is because an open bidding process would give all concerned the most information possible about both the value of the license at issue in any given auction and about the opportunities for other such licenses. During an auction, a prospective PCS

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<sup>20</sup> *Auctioning Radio Spectrum Licenses* at 44.

<sup>21</sup> *See Auctions and Bidding* at 725.

<sup>22</sup> Maximizing revenues is not permitted to be the sole or predominant purpose of spectrum auctioning, *see* 47 U.S.C. § 309(j)(7)(B), whereas that is generally the case in other auctions. In addition, OBRA requires the Commission to continue to encourage negotiations and similar techniques to eliminate mutual exclusivity among applicants, which would eliminate the need for auctions. 47 U.S.C. § 309(j)(6)(E). Thus, Congress has urged the Commission to permit negotiations among applicants to reach agreements that might, under other circumstances, constitute collusion. Moreover, to encourage negotiations among applicants, the Commission would have to take steps contrary to those it would take to minimize the possibility of collusion. For example, to prevent collusion, the Commission would avoid identifying bidders in advance, but to encourage negotiations it would have to make bidders' identities known.

<sup>23</sup> 47 U.S.C. § 309(j)(3)(B) and (4)(D).

participant would be able to refine its valuation of a particular license in light of other parties' bids. Thus, a less-informed bidder would have a measure of protection from making an unrealistically high bid, but would also have the ability to decide that a license has a higher value than previously believed.<sup>24</sup> Moreover, the information made available through open bidding would serve to educate prospective bidders about other companies' valuations in previous auctions.<sup>25</sup>

The most important way to provide new entrants with an opportunity to bid meaningfully is to use an auction process that maximizes this flow of information. Companies already involved in a field have a substantial knowledge base that they can fall back on in devising a bidding strategy. They know who else is involved in their field, and they have the ability to estimate the probable value of a license. They would have a significant advantage over newcomers if sealed bids are used.

New entrants may not have access to such information, as newcomers to wireless services, and accordingly some small and minority- or female-owned businesses and rural telephone companies, could be at an information disadvantage in a sealed-bid auction. An open bidding process would be particularly beneficial to new entrants by educating them about others' valuations of a license during the bidding for a license. Moreover, studying the bids of others in past auctions would open opportunities that otherwise might not be available to them. For example, a small or minority-owned business might be able to use this information to predict that there would be few bidders for a given license, or that the probable winning bid for that license would be affordable, based on the approach taken by others with regard to similar licenses. Or a rural telephone company might be able to use such information to decide on a strategic partner for a license in its community.

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<sup>24</sup> The auction winner knows, for example, that the second-highest bidder valued the license at or near the final bid price. If there are no significant restrictions on resale, therefore, this would give the winning bidder some information as to what the secondary-market value of the license might be.

<sup>25</sup> Before a given auction, potential bidders would have access to information about the number and identity of parties bidding in previous auctions for similar licenses and the size of their bids. A potential bidder could use this information to infer the value placed on the licenses in a prior auction.

The use of sealed bids would disadvantage these new entrants and thereby lessen the variety of businesses participating in the auctions. To promote the statutory objective of promoting economic opportunity and competition, the Commission should adopt the auction method most conducive to new entry: open auctions.

The Commission should design its auction process to heighten awareness about new licensing opportunities among businesses that otherwise might not be sufficiently informed to participate.<sup>26</sup> These efforts, coupled with open eligibility standards that would not exclude *any* potential service provider, will result in the broadest possible variety of bidders and will maximize competition in the provision of PCS.

### **3. Open Auctions Are Simple to Administer and Would Avoid Administrative and Judicial Delay**

Open auctions have a considerable advantage over other bidding systems in that they are the simplest way of carrying out an auction. Open auctions are well understood by all concerned and would not require the development of complex rules. Moreover, if auctions are conducted openly, there is no need for security precautions to protect the secrecy of the written bids before opening.

Open auctions also have an advantage over sealed bids in terms of the statutory objective of avoiding administrative and judicial delay, when, as here, there are multiple licenses for a given service area being auctioned. Specifically, the outcomes of the several auctions for licenses in a given area are interdependent. A bidder may wish to participate in multiple auctions for the licenses for a given area, in the hope of winning one. However, the bidder may not be willing to pay for (or may not be permitted to hold) more than one such license. If open auctions are used, the bidder will file applications for each license and participate in each auction until the bidder wins or all of the

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<sup>26</sup> Such outreach opportunities might go beyond measures the Commission has already taken, such as seminars and "brown bag" luncheons for target groups. For example, the Commission might undertake to publish articles or notices concerning new services and licensing opportunities in magazines, newsletters, and newspapers widely read among small businesses, minority and female-owned businesses, and telephone companies serving rural communities.

auctions are concluded. If sealed bids are used, however, the bidder's bids in each of the multiple auctions would have to be contingent on the outcome of the other auctions. Resolution, after the fact, of which bids were appropriately considered is likely to result in litigation and delay development of the service. While rules could be adopted to address such contingencies, the opportunity for manipulation and the potential for consequent litigation remains. Accordingly, this statutory objective appears to provide additional support for using open auctions.

**B. The Commission Should Contract With an Experienced Auction House to Conduct the Auctions**

Because the Commission does not have any experience in devising and conducting auctions, it would be highly desirable to contract with an qualified auction house to conduct the auctions. This would have several advantages. First, the Commission would not have to train its staff to conduct auctions or establish detailed rules and administrative directives to govern the process. This would entail significant cost and time savings. Second, practically no staff resources or space would have to be devoted to conducting auctions. Third, the use of an outside auctioneer would permit the auction to be conducted at no cost to the government.<sup>27</sup> Finally, the use of an experienced auction house would result in auctions that are conducted expertly and therefore result in maximum financial benefit to the government.

**C. The Commission Should Require a Reasonable Deposit to Participate in an Auction**

The integrity and efficiency of the auction process requires that steps be taken to ensure that only *bona fide* bidders be permitted to participate. Specifically, all bidders must be willing to be bound by the outcome and all bidders must be able to satisfy their obligations should they win. The

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<sup>27</sup> Auction houses typically are paid for their services by either a commission deducted from the winning bid, a premium paid on top of the winning bid, or a combination of the two. A buyer's premium paid directly to the auction house would appear to be an adequate way to compensate the auctioneer.



first of these concerns can be addressed by requiring all bidders to include an appropriate certification as part of their pre-auction application.<sup>28</sup>

A certificate does not supply reasonable assurance that the winning bidder will be able to satisfy its financial obligations, however. For that reason, the Commission should require each bidder to post a deposit prior to the auction that provides assurance of the bidder's *bona fides*. The size of the deposit should vary with the nature of the license being auctioned, within reasonable limits. How large the deposit should be in relationship to bidding capacity should be set for comment. BellSouth suggests that for PCS, a deposit of \$10 per 1,000 inhabitants of the service area, with a \$1,000 minimum, would be an appropriately sized deposit. The deposit should be refundable to those not winning the auction.

## **II. EACH LICENSE IN A RADIO SERVICE SHOULD BE AUCTIONED SEPARATELY, IN DESCENDING ORDER OF POPULATION SERVED, IN A RELATIVELY SHORT TIME FRAME**

The Commission should give the public clear notice of the sequence that is to be followed in holding auctions. Specifically, BellSouth urges the Commission to hold separate auctions for each of the licenses in any given radio service, in descending order of the population that may be served by each license.<sup>29</sup> The Commission should schedule auctions for all of the various licenses in a service such as PCS at relatively close intervals. This would permit the Commission to auction all of the licenses for all areas within a reasonable time frame, and avoid the considerable time lag in progressing beyond the large markets that has occurred in cellular and other services.

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<sup>28</sup> The bidders should, at a minimum, certify that they are participating in good faith, that they agree to be bound by the outcome, that their specified representatives have full authority to act in their behalf, and that they have the ability to comply with any financial obligations they incur.

<sup>29</sup> Of course, in radio services where the Commission does not designate the particular service areas to be applied for, but permits applications to be filed for service areas determined on an ad hoc basis, based on the extent to which such applications may be interleaved with existing facilities, there would be no such sequence. In these cases, the auctions should follow the sequence established by the cut-off dates for the filings.

The most populous areas are, in general, the areas with the greatest unsatisfied demand for existing services. These areas can be expected to have a high level of demand for new services, as well.<sup>30</sup> Furthermore, there appear to be important business reasons for licensing the major population centers first, in that coverage of these markets will require the largest investment.

In some services, the Commission may decide to license several blocks of spectrum separately in each market. In these cases, bidders should be permitted to file applications for each of the blocks on the same date without regard to any limitations imposed by the rules on multiple holdings. If there are mutually exclusive applications filed, separate auctions would be held for each block. An applicant would be permitted to bid for each block that would be separately licensed as long as the bidder would not exceed the established limit by winning.

This is preferable to holding a single auction for all of the frequency blocks to be licensed in a particular market for several reasons. There may frequently be significant technical differences between the blocks that would affect each bidder's valuation of, or willingness to bid for, the various blocks.<sup>31</sup>

In some services, the Commission has defined several different overlapping service areas to be licensed on separate frequencies or channels, such as Narrowband PCS, where there are national, regional, and local channels. In these cases, the Commission should proceed according to the same sequence: hold auctions for the licenses serving the most population first. In the case of

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<sup>30</sup> For example, in the case of PCS, the demand for new low-powered, pedestrian-oriented services is expected to be greatest in major urban areas.

<sup>31</sup> For example, there may be incumbent co-channel or adjacent-channel licensees that are entitled to interference protection in the case of one frequency block, while a second block is entirely clear. Also, some applicants may have a technical reason for needing one particular frequency block, such as integration into a multi-market network on the same frequency block. Another reason for auctioning the frequency blocks separately is that in some services, where the rules permit holding multiple licenses in a given area (such as Narrowband PCS), bidders may be bidding for different numbers of licenses. Complex rules would be needed to determine how to proceed in such cases, if multiple channels or frequency blocks were auctioned together.

Narrowband PCS, the national licenses would be auctioned first, followed by regional and local licenses in declining order of population.

Absent compelling technical justifications, BellSouth submits that the statutory objective of encouraging competition and participation by a wide variety of businesses would be served by adopting rules that establish relative parity among the licenses for a given area, and avoiding the use of different overlapping service area designations or different frequency block sizes. For example, if the Commission were to use national, regional, and local service areas for licensing Wideband PCS, entrants such as minority- and female-owned businesses and rural telephone companies could be disadvantaged. The national and regional service areas would be fewer in number than the local service areas. Companies already in related fields would tend to value the licenses for larger service areas more highly, leaving for others only the least valuable licenses with the lowest ability to provide a competitive alternative. Similar results would be expected if the Commission were to issue licenses for several different spectrum block sizes for a given service area.

To maximize the opportunity for open entry and to give everyone the opportunity to compete equally, the Commission should seek to establish parity among the various competing licenses in any given service. In other words, the licenses should be for the same area and the same amount of spectrum.

### **III. THE COMMISSION SHOULD GIVE ALL WINNING BIDDERS THE OPTION OF PAYING IN A LUMP SUM OR IN INSTALLMENTS**

Congress required the Commission to consider "alternative payment schedules and methods of calculation" that would allow winning bidders to satisfy their obligations in various ways.<sup>32</sup> The Commission is given wide rein: Among the alternatives for consideration are "lump sums or guaranteed installment payments, with or without royalty payments, or other schedules or methods

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<sup>32</sup> 47 U.S.C. § 309(j)(4)(A).

that promote the objectives described in [47 U.S.C § 309(j)(3)(B)], and combinations of such schedules and methods."

For PCS, BellSouth urges the Commission to adopt rules providing only for lump-sum and installment payments. These are relatively straightforward and can be adopted without delay. Royalties, on the other hand, would be inappropriate for PCS auctions, because they would be difficult to implement,<sup>33</sup> they would tend to lower federal revenues from auctions in both the short and long term, and they would give licensees an incentive to defer expansion of service capacity until after the royalty period, to avoid paying royalties.

Lump-sum payments would be simple to implement. The winner would be obliged to pay the entire bid amount before a license is granted. Failure to do so within a fixed time period after the winner's qualifications are established would result in dismissal of the winner's application.

Installment payments would also be relatively simple to implement. The winner would be obliged to sign a promissory note, supply any necessary guarantees, and make a down payment before a license is granted. As with the lump-sum payment, the winner's failure to comply would result in dismissal.

The Commission should adopt rules specifying the size of any required down payment and the terms of any permissible installment payment plan. In reaching this decision, it should consider several types of installment plans. BellSouth recommends that any installment plan for PCS be designed to recoup the value of the license within a term of no more than five years.<sup>34</sup> The

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<sup>33</sup> It would be difficult to establish a bidding mechanism that fairly evaluated one bidder's royalty proposal vis-à-vis another. Comparing royalty bids might even require a miniature comparative hearing just to determine the winning bid, because determining which bidder was highest would require a comparison of business plans (e.g., determining relative demand estimates, ability to accommodate demand, coverage, expansion plans, services, and rates, as well as the quality of revenue assumptions).

<sup>34</sup> This is necessary because the grant of auction authority in OBRA was specifically intended to result in substantial revenues from PCS auctions in Fiscal Years 1994-1998. The FCC will commence issuing PCS licenses after the middle of Fiscal Year 1994, and some licenses may not be issued until later in Fiscal Year 1994, or even Fiscal Year 1995. In order to ensure that the bulk of the revenues from PCS license auctions  
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following alternatives may be considered in determining the type of payment plans to incorporate in the rules:

- (1) A fully amortized schedule of equal payments (principal and interest) at a fixed simple interest rate;
- (2) A fully amortized schedule of variable payments (principal and interest) at a floating simple interest rate;
- (3) A schedule of equal payments (principal and interest) at a floating simple interest rate, with a balloon payment at the end of the term if principal remains to be paid; and
- (4) A graduated schedule calling for interest payments with increasing principal payments starting after a fixed number of payments, at a fixed or floating interest rate.

The graduated schedule would be particularly advantageous to businesses that may not be highly capitalized, including small businesses and minority- or female-owned businesses. It would minimize the payments required during the initial years of the license, when the licensee will have substantial negative cash flow due to construction of the system, and calls for the highest payments after the system has had time to build a subscriber base and income stream. In any event, any alternative payment plan that is incorporated into the rules should be available to any auction winner.<sup>35</sup>

As required by Congress, any installment payment plan must provide for appropriate guarantees of payment. The Commission should scrutinize the financial ability of any guarantors carefully to prevent defaults, which would both unjustly enrich the license holders and deprive the nation of needed revenues.

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<sup>34</sup>(...continued)

are received during the time frame Congress intended, the installment payment schedule should be no longer than five years. Indeed, the Commission should consider the use of payment schedules that will result in full payment by September 30, 1998.

<sup>35</sup> Making alternative payment plans available only to particular types of auction winners would encourage non-qualifying entities to use qualifying entities as their "fronts" in bidding. This would result in a significant number of legal controversies and would also unjustly enrich both the front groups and their sponsors. It would also require very close scrutiny of any transfer or assignment applications by the licensees using such payment plans to determine whether there have been such abuses.

The Commission should also address the consequences of a licensee defaulting on payments due under an installment plan. A defaulting licensee would be unjustly enriched by being able to continue holding its license. The Commission should not have to undertake lengthy revocation hearings to reclaim a license from a defaulter. Accordingly, BellSouth recommends that any license grant to an auction winner choosing to pay on an installment plan be conditioned on meeting all payment obligations. The rules should provide that upon default, the license grant automatically becomes voidable; if the licensee does not pay all overdue amounts plus an appropriate penalty<sup>36</sup> within 15 days of the notice of default, the license would automatically be canceled without a hearing.<sup>37</sup>

#### **IV. AFTER AN AUCTION, THE COMMISSION SHOULD NOT UNDULY RESTRICT TRANSFERS AND ASSIGNMENTS OF LICENSES**

The Commission should not adopt significant restrictions on transfers of control and assignments of licenses, such as holding periods or restrictions on sale of an unconstructed system, after award of licenses by auction. If there is broad participation in the auction and the Commission has not facilitated abusive behavior by adopting preferential rules, an auction will result in award of a license at, or close to, fair market value. Under these circumstances, there will be no incentives to engage in "trafficking," "warehousing," or similar activities. A licensee will be obliged to use the license (*i.e.*, comply with any construction and build-out requirements) in order to maintain its value.

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<sup>36</sup> The penalty should be significant, such as 1.5 percent of the outstanding principal balance for each month of default.

<sup>37</sup> The Commission should also determine the effect of such cancellation on the amount remaining outstanding on the defaulter's note. It would clearly not be appropriate for any further obligation to be cancelled, because this would give speculative applicants an incentive to make overly-high bids; if the license does not become as valuable as the licensee had hoped, it would be able simply to walk away from its obligation. At a minimum, the licensee should remain obligated to make its remaining installment payments. The Commission should consider, however, whether the outstanding balance on the note should be accelerated, becoming due and payable in full upon cancellation of the license.

The fair market value of a license may change after an initial grant, however, due to the introduction of new technologies, competitive conditions, or other market conditions. Another entity may come to value the license more highly than the licensee, for example. As a result of such changes, or because of changes in a licensee's own financial condition or business plans, there will be situations where an assignment or transfer of control is appropriate. The Commission should not adopt rules or policies that interfere with such transactions but should instead permit the marketplace to function, provided that the assignee or transferee is found qualified pursuant to 47 U.S.C. § 310(d).

The Commission should not permit assignments of licenses to be used as a way around installment payment obligations. There are two ways to accomplish this. The preferred option would be to accelerate payment of any installment note upon assignment of license; grant of consent for a transfer of control would be conditioned on paying the entire balance due on the note prior to consummation. As an alternative, the Commission may wish to permit an installment plan to be assumable. In this case, it should not release the original obligor until the obligation has been satisfied in full.<sup>38</sup> In a transfer of control, the licensee does not change, so such rules should not generally be applicable to transfers.<sup>39</sup>

Finally, the Commission should adopt rules requiring review of any assignment of license or transfer of control involving a license obtained by auction to ensure against an abuse of the auction process or unjust enrichment. Such abuses might include the use of "fronts" to take advantage of

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<sup>38</sup> The parties should not be prohibited, however, from contracting among themselves or with third parties to redistribute any financial liabilities. Thus, parties would be free to enter into indemnification, hold-harmless, and guarantee agreements or insure against liability. Such agreements would permit parties to arrive at reasonable business arrangements that might require a seller's obligation to be extinguished effectively.

<sup>39</sup> The Commission may find it necessary to adopt rules regarding substitution of guarantors, however. If a transfer of control resulted in a change of guarantors, because an owner of the licensee had guaranteed payment, the Commission should review the transfer of control to ensure that any such change of guarantors complies with its rules.

preferential rules<sup>40</sup> or to facilitate collusive bidding.<sup>41</sup> Because of the variety of such abuses, it would probably be counterproductive to adopt specific rules as to how such review will be conducted.

**V. LICENSEES FAILING TO MEET REASONABLE MINIMUM CONSTRUCTION OR COVERAGE REQUIREMENTS SHOULD FORFEIT THEIR LICENSES AUTOMATICALLY, ABSENT GOOD CAUSE, AND SHOULD REMAIN LIABLE FOR ANY INSTALLMENT PAYMENTS OWED**

The Commission should, in separate proceedings for each radio service, adopt rules regarding the minimum build-out requirements (e.g., schedules for minimum required construction and/or coverage) that a licensee must meet, to the extent such rules do not already exist. These rules would address concerns that auction winners will simply "warehouse" frequencies and prevent their beneficial use.<sup>42</sup> The rules should specify only the minimum required to ensure that the spectrum is utilized consistent with the public interest and not merely warehoused. Licensees should be given the ability to scale their services to the demands of the marketplace.

The Commission should adopt rules providing that a licensee selected by auction who fails to satisfy its build-out obligations will forfeit its license automatically, absent a showing of good cause.<sup>43</sup> To give licensees the greatest incentive to comply with their obligations and to avoid

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<sup>40</sup> BellSouth urges the Commission not to adopt preferential rules, such as bidding preferences, set-asides, or eligibility restrictions for alternative payment plans because they will create incentives for abuse. By refraining from adopting such rules, the Commission will avoid the need to scrutinize assignments and transfers for abuse.

<sup>41</sup> If a cartel succeeds in obtaining a license at a below-market price at auction through collusive practices, it may subsequently seek to assign that license to a cartel member at a higher, but still below-market, price. *Auctions and Bidding* at 724-25.

<sup>42</sup> Theoretically, such rules should not be necessary, because the usage value conferred by a radio spectrum assignment cannot be accumulated. Each day that a commercial license remains unused represents foregone revenue. Thus, a licensee will generally lose value by not using a license. There may be circumstances, however, where the long-term strategic value of a spectrum assignment is far greater than the present value of the revenue stream. In such rare circumstances, a construction, coverage, or build-out requirement would serve the public interest objective of ensuring that the spectrum is used to provide service to the public more promptly.

<sup>43</sup> The Commission should adopt rules permitting a licensee to request a waiver for good cause reasonably in advance of a scheduled compliance date. For example, a licensee may be unable to comply with  
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abuses, the license should be forfeited in its entirety.<sup>44</sup> Under these circumstances, market forces, aided by this regulatory spur, would make the build-out requirements largely self-actualizing.<sup>45</sup>

Congress required the Commission to structure its rules so as to prevent unjust enrichment of those obtaining licenses by auction. Accordingly, the Commission should adopt rules that, at a minimum, make clear that forfeiture of one's license does not excuse any payments due under an auction installment note. It may be appropriate to go even further, however, and establish that any outstanding installment obligations will be accelerated and due immediately in full upon forfeiture of license.

## **VI. A STREAMLINED LICENSING PROCESS SHOULD BE USED**

The institution of auction procedures gives the Commission the opportunity to redesign its licensing process for efficiency. Congress required that the rules adopted by the Commission to

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<sup>43</sup>(...continued)

a geographic coverage requirement because of its inability to obtain usable transmitter locations despite reasonable efforts. (Large areas of land may be unavailable for commercial use or unsuitable for transmitter locations due to environmental or other restrictions; zoning restrictions and land-use planning requirements may preclude use of essential locations or require lengthy approval, variance, or waiver processes.) Equipment development for a new service may be delayed by the manufacturer chosen by the licensee. A new technology may have unexpected disadvantages that make compliance with the schedule inadvisable. An incumbent fixed microwave licensee may delay negotiations with a PCS licensee, using the PCS licensee's build-out schedule as leverage. Weather conditions, interest rates, or other unpredictable factors may also impede a licensee's ability to meet the required schedule in unforeseeable ways

<sup>44</sup> A licensee that fails to meet the Commission's build-out requirements should not be allowed to retain its license in part (e.g., for a reduced license area or smaller number of channels). Otherwise it may be economically desirable to sacrifice the noncompliant part of a licensed area if the cost of compliance is greater than the marginal value of the portion of the licensed area that would be forfeited. For example, a licensee with 50% population coverage might make the decision to ignore a 75% coverage requirement and forfeit any right to cover beyond the 50% coverage area, if the cost of adding an additional 25% population coverage would be greater than the loss in value suffered by restricting the scope of its license. Furthermore, a licensee might be willing to undertake the cost of an appeal of the partial forfeiture if the cost of the appeal is low compared with the value of the forfeited part of its license.

<sup>45</sup> A licensee approaching a deadline who will be unable to comply with such a requirement will have an incentive to sell at a depressed price to another party who will be able to meet the requirement, rather than to lose the entire value of the license.